MCI Telecommunications Corporation

1801 Pennsylvania Ave., N.W.
Washington, D.C. 20006
202 887 2372
FAX: 202 887 3175

Frank W. Krogh
Appellate Counsel
Regulatory Law

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June 19, 1995

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Mr. William F. Caton
Secretary
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

Re: Price Cap Regulation of Local Exchange Carriers; Rate-of-Return Sharing and Lower Formula Adjustment, CC Docket No. 93-179

Dear Mr. Caton:

MCI Telecommunications Corporation (MCI) wishes to take this opportunity to respond to certain aspects of the Reply of Ameritech to Opposition to Emergency Motion for Stay filed herein on May 15, 1995. This response is necessitated by mischaracterizations in Ameritech's Reply that may leave the record unclear if not corrected.

First, Ameritech tries to support its argument that the "Add-Back Adjustment" Order (Order)[1/] is illegally retroactive by reference to a false analogy to income tax liability. Ameritech argues that the Order is retroactive in effect because it alters sharing obligations arising from past earnings, comparing the Order to a hypothetical IRS decision in early 1995 to eliminate a deduction applicable to 1994 income taxes.

The problem with Ameritech's analogy, however, is that 1994 income taxes must be paid in 1994, either quarterly or through withholding. An IRS decision in 1995 affecting 1994 deductions thus has legal consequences for 1994, not just on April 15, 1995. With regard to a LEC's sharing obligations, however, a LEC's earnings in year 1 only have legal consequences for year 2, during which those earnings must be shared through rate

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[1/] Price Cap Regulation of Local Exchange Carriers; Rate-of-Return Sharing and Lower Formula Adjustment, CC Docket No. 93-179, FCC 95-133 (released April 14, 1995).

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reductions. There are no legal consequences from a certain level of earnings apart from the sharing obligation incurred thereby in the following year.

More importantly, as MCI explained in its Opposition to Ameritech's Emergency Motion for Stay, filed on May 5, 1995, as well as in its Petition for Reconsideration of the Order, filed on May 24, 1995, there is nothing new about the add-back adjustment codified in the Order.[2/] Such an adjustment was at least implicit in the regulatory scheme established in the LEC Price Cap Orders.[3/] Nothing in those Orders suggested or implied that the Commission would not continue to exclude the impact of amounts returned to ratepayers in measuring actual current earnings from current operations. Sharing, like a refund, is not a cost of providing service, but, rather, reflects previous results. Thus, the add-back adjustment spelled out in the Order simply codifies long-standing practice and cannot be considered retroactive, even as applied to the 1993 and 1994 annual access filings.

Moreover, Ameritech was given explicit notice that the Commission might well apply an add-back adjustment, long before release of the Order. The Commission tentatively concluded in its Notice of Proposed Rulemaking initiating this docket (NPRM) that price cap LECs should continue to be required to add back sharing and low-end adjustments in measuring current rate of return, since that approach was more consistent with previous Commission practice and with the nature of sharing as a one-time adjustment.[4/] The Commission issued a similar warning when it initiated an investigation as to the same issue with respect to the 1993 and 1994 annual access tariff filings.[5/] The Order itself thus cannot be considered retroactive in any meaningful sense, since it does not effect a regulatory change. Contrary to Ameritech's claim, the Order "leaves intact the reasonable

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[2/] A copy of MCI's Petition for Reconsideration is attached hereto as Exhibit A.

[3/] Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, 5 FCC Rcd 6786 (1990) (LEC Price Cap Order), Erratum, 5 FCC Rcd 7664 (Com. Car. Bur. 1990), modified on recon., 6 FCC Rcd 2637 (1991) (LEC Price Cap Recon.), aff'd sub nom., National Rural Telecom Ass'n v. FCC, 988 F.2d 174 (D.C. Cir. 1993).

[4/] 8 FCC Rcd 4415 (1993).

[5/] See 1993 Annual Access Tariff Filings, 8 FCC Rcd 4960, 4965, 4973 at ¶¶ 32, 105 (Com. Car. Bur. 1993) (1993 Annual Access Order); 1994 Annual Access Tariff Filings, 9 FCC Rcd 3519, 3523-24 at ¶ 7 (Com. Car. Bur. 1994).

expectations carriers and the public have formed based upon the Commission's existing rules...."[6/]

Accordingly, Ameritech's argument that it would have chosen a different productivity factor in its 1993 annual access charge filing must also be rejected. It should be noted that both the NPRM and 1993 Annual Access Order were adopted, and the latter was released, in late June, 1993, prior to the effective date of the 1993 annual access tariffs. Ameritech thus cannot claim that it was locked into its choice of productivity factor when it received those additional warnings that its approach to earnings measurement might not be accepted.

Ameritech is also wrong as to the nature of its alleged injury in the absence of a stay. Ameritech argues that the out-of-period adjustment authorized by Section 65.600(d)(2) of the Commission's Rules would not allow it to recover, in its 1996 annual access filing, the additional sharing amounts resulting from the add-back adjustment in the event that it ultimately prevails in its challenge to the Order. There is nothing in Section 65.600(d)(2) to suggest such a narrow interpretation, however. It states that price cap LECs "shall file with the Commission within fifteen (15) months after the end of each calendar year a report reflecting any corrections or modifications to the [final rate-of-return] report." Ameritech is certainly correct that MCI's main concern in raising this issue in the LEC Price Cap proceeding was to capture, for sharing purposes, any increase in earnings resulting from post-period adjustments, but nothing in the LEC Price Cap Orders or Section 65.600(d)(2) limits the scope of that provision to upward adjustments. Ameritech thus will be free, if it should prevail in its challenge to the Order, to increase its PCI in its 1996 annual access tariff to recover the additional sharing carried

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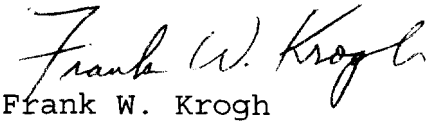
[6/] Ameritech Reply at 9. In fact, because the add-back adjustment implicitly flows from the price cap scheme, "and simply made explicit what was implicit...from the beginning," the Order could have been issued as an interpretive rule, without notice and comment. Pennzoil Co. v. DOE, 680 F.2d 156, 176 (TECA 1982), cert. dismissed, 459 U.S. 1190 (1983). See also Metropolitan School District of Wayne Tp. v. Davila, 969 F.2d 485 (7th Cir. 1992), cert. denied, 113 S. Ct. 1360 (1993); Chemical Waste Management, Inc. v. USEPA, 869 F.2d 1526 (D.C. Cir. 1989); National Helium Corp. v. FEA, 569 F.2d 1137, 1145-46 (TECA 1977); Energy Reserves Group, Inc. v. DOE, 589 F.2d 1082, 1091-1100 (TECA 1978), cert. denied, 469 U.S. 1077 (1984).

out in its 1995 access rates resulting from the application of the add-back adjustment to its 1994 earnings.[7/] It must be concluded that Ameritech cannot show the immediate, irreparable injury required for a stay.

Yours truly,



Frank W. Krogh

Attachment

[7/] MCI also agrees with Ameritech that such recovery by Ameritech will not present issue of retroactive ratemaking if the Commission, in denying a stay of the Order, explicitly states now that Ameritech will be permitted to adjust its 1996 annual access rates as discussed above in the event its challenge to the Order is successful.

Exhibit A

MCI Telecommunications
Corporation
1801 Pennsylvania Avenue, N.W.
Washington, D.C. 20006

May 24, 1995

Mr. William F. Caton
Secretary
Federal Communications Commission
Room 222
1919 M Street, NW
Washington, DC 20554

Re: CC Docket No. 93-179; Price Cap Regulation of Local Exchange Carriers; Rate of Return Sharing and Lower Formula Adjustment

Dear Mr. Caton:

Enclosed herewith for filing are the original and four (4) copies of MCI Telecommunications Corporation's Petition for Reconsideration in the above-captioned proceeding.

Please acknowledge receipt by affixing an appropriate notation on the copy of the MCI comments furnished for such purpose and remit same to the bearer.

Sincerely yours,

Chris Frentrup
Senior Regulatory Analyst
Federal Regulatory

Enclosure
CF

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20054

In the Matter of	)	
	)	
Price Cap Regulation of	)	
Local Exchange Carriers	)	CC Docket No. 93-179
	)	
Rate-of-Return Sharing	)	
and Lower Formula Adjustment	)	
	)	

PETITION FOR RECONSIDERATION

I. INTRODUCTION

Pursuant to Section 1.106 of the Commission's rules, MCI hereby submits its petition for reconsideration of the Add-Back Order in the above-captioned docket.[1] Although MCI applauds the Commission's decision to require add-back, MCI believes that the Commission was incorrect in its determination that it could not make "add-back" retroactive to the beginning of price caps. MCI urges the Commission, for the reasons set out herein, to make add-back retroactive to the first annual access filing in which add-backs would have been implemented, i.e., 1993.

II. BACKGROUND

The Commission adopted price caps for the local exchange carriers (LECs) effective on January 1, 1991. As part of that regulatory scheme, the

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[1] In the Matter of Price Cap Regulation of Local Exchange Carriers; Rate of Return Sharing and Lower Formula Adjustment, CC Docket No. 93-179, Report and Order, FCC 95-133, released April 14, 1995 (Add-Back Order).

Commission adopted a backstop sharing and low-end adjustment mechanism. These features of the plan required prospective adjustments to a LEC's Price Cap Indexes (PCIs) if the LEC's earnings in the previous calendar year exceeded certain levels.

The first application of the sharing and low-end adjustment mechanisms occurred in the 1992 annual access filing. The first annual access filing in which the issue of whether add-back was required thus arose in the next annual filing, in 1993. In that filing, several carriers computed their earnings without the add-back, and one carrier computed its earnings with the add-back. The Commission suspended those rates and instituted an investigation into whether add-back was required.[2] The Commission also adopted the NPRM in this docket shortly before those tariffs took effect, to examine the general issue of add-back adjustments.[3] The tariff investigation is still pending.

III. FAILURE TO MAKE ADD-BACK ADJUSTMENTS RETROACTIVE IS INCONSISTENT WITH THE COMMISSION'S FINDINGS IN THE ADD-BACK ORDER

In the Report and Order of which MCI now seeks reconsideration, the Commission makes, inter alia, two findings. The first of these is "...an add-back requirement is not only full consistent with, but also an essential element

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[2] 1993 Annual Access Tariff Filings, 8 FCC Rcd 4960 Com. Car. Bur. 1993); see also 1994 Annual Access Tariff Filings, 9 FCC Rcd 3519 (Com. Car. Bur. 1994) (adding the 1994 access rates to the 1993 investigation of add-backs).

[3] Price Cap Regulation of Local Exchange Carriers, Rate of Return Sharing and Lower Formula Adjustment, 8 FCC Rcd 4415 (1993) (NPRM).

of, the system of price cap regulation that we adopted for LECs in 1990."[4] The Commission then notes that "... the Commission did not state that it intended to eliminate the requirement under rate-of-return regulation that carriers subtract revenues reflecting out-of-period earnings for purposes of calculating current year earnings."[5] The second finding the Commission made is that requiring add-back adjustments "...does not constitute a major change to the LEC price cap rules."[6]

As the Commission rightly points out, add-back was the status quo for computation of the LECs' rate of return under rate-of-return regulation, and nothing in the Commission's LEC price cap decision amended or modified those computation requirements in any way. Absent any Commission direction to the contrary, therefore, there could be no expectation that the Commission's existing add-back requirement would have disappeared.

The Commission's finding that it can apply its new rule requiring add-back only prospectively is thus inconsistent with findings the Commission made in its Add-Back Order. MCI argues that the rule the Commission adopted is not a new rule; it is merely a codification of long-standing, and prior to the advent of price cap regulation, unopposed Commission practice. MCI urges the Commission on reconsideration to require the retroactive application of add-

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[4] Add-Back Order at para. 32.

[5] Id.

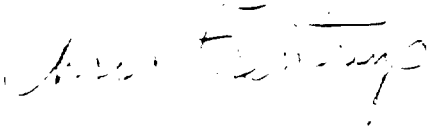
[6] Id. at para. 50.

back adjustments.[7]

IV. CONCLUSION

The Commission made the correct finding that add-back adjustments are an integral part of the Commission's price cap plan. However, the Commission erred when it declined to make the application of this decision retroactive to the beginning of price caps. For the reasons stated herein, MCI urges the Commission, on reconsideration to apply its add-back requirement retroactive to the beginning of price cap regulation.

Respectfully submitted,
MCI TELECOMMUNICATIONS CORPORATION



Chris Frentrup
Senior Regulatory Analyst
Federal Regulatory
1801 Pennsylvania Avenue, NW
Washington, DC 20006
(202) 887-2731

May 24, 1995

[7] Given the Commission's statements in this docket, MCI sees no way the Commission can find in its on-going investigation into the 1993 and 1994 annual access tariff filings that add-back adjustments do not apply.